

2015 Advisory Council on Employee Welfare and Pension Benefit Plans
Model Notices and Disclosures
For Pension Risk Transfers

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Description of Issue:

In recent years, there has been a noticeable increase of activity by single-employer defined benefit (DB) pension plans, to offer lump sum distributions to some or all of their participants, many times with a limited election window (lump sum risk transfers). Lump sum risk transfers shift the risk related to lifetime retirement benefits from the plan to the participants. Other transactions involve the purchase of a group annuity contract by the plan from an insurance company (insurance annuity risk transfer), which transfers the risk from the plan to the insurance company. In the past, this activity has been referred to as “derisking,” which takes the perspective of the plan/plan sponsor that has transferred its risk to a third party, usually an insurer. More accurately, these transactions are referred to as “risk transfers,” which is the term that will be used in this scope statement.

In 2013, the Council conducted a comprehensive study of the risk transfer process. The 2013 Council report included, among other things, recommendations regarding the information needed by plan participants involved in risk transfer transactions. For lump sum risk transfers, the 2013 Council recommended improved participant disclosures in the following areas: (1) Limit election windows to no less than 90 days; and (2) Include “relevant information to enable a participant to make an informed election” concerning such issues as the potential impact of tax penalties, whether an early retirement subsidy is included in the lump sum, and a comparison of the lump sum to other benefits under the plan.

The 2015 Council will supplement the work of the 2013 Council by focusing specifically on the information that participants need to make informed decisions when faced with lump sum risk transfers and insurance annuity risk transfers, and best practices for plan sponsors in communicating that information. The goal of the 2015 Council is to offer the Department of Labor draft model notices and disclosures that can be used by plan sponsors, participants, and the public.

Objective and Scope:

We are interested in learning about the problems that participants have with understanding choices in risk transfer transactions. However, our primary focus is on the solutions instead of the problems. Therefore, witnesses will be asked to address the following question:

What useful information do participants need to make an informed decision in a risk transfer transaction, and how would you suggest getting this information to participants? We intend to focus witness testimony on this basic question.

The Council is examining this topic and intends to draft recommendations to the Secretary of Labor for consideration. Our study will include the following:

- A. Review of existing regulations on notices/disclosures/elections/waivers already in use in related contexts and whether they are adequate and understandable by the participant.
- B. Review of the findings in the GAO 2015 Report related to the relevant information that participants need to consider when faced with lump sum risk transfers, the adequacy of disclosures to participants, and which information that plan participants found useful.
- C. Review of plan sponsor informational packets from prior lump sum risk transfers and insurance annuity risk transfers.
- D. Draft illustrations and examples to compare the value of an ERISA pension plan annuity to a retail insurance annuity purchased with the lump sum amount under current market conditions, and study the information that the participant needs to understand the economic difference between the two.
- E. Study the extent to which behavioral science predicts how people will react when presented with lump sum risk transfers and insurance annuity transfers and the lessons that can be learned.
- F. Determine the extent to which plan fiduciaries should take into account the individual circumstances of participants, such as elderly retired participants with an increased likelihood of diminished capacity and who may be subject to undue influence by advisers.
- G. Invite interested parties to submit model disclosures, notices, and informational packets for lump sum risk transfers and insurance annuity risk transfers, and to provide advice on the best practices and experience with different media (meetings, websites, video, etc.).
- H. Study the types of communications and disclosures that are provided to different participant populations, and the most effective method of delivery of the information. Examples of different participant populations receiving different communications may include retirees receiving notice of an annuity purchase, terminated vested participants being offered a lump sum option, and active participants receiving notification of a plan change or risk transfer action that could affect them.

- I. In the case of lump sum risk transfers, study disclosures that are needed to communicate the consequences of choosing a lump sum in lieu of future benefits payable from the pension plan and the risks the participant takes on with such an action (e.g. longevity and investment risk).
- J. In the case of a group annuity purchase by the pension plan sponsor, consider the disclosures needed to communicate differences between annuities offered under the ERISA pension plan and annuities provided by an insurer, including the different protections offered under ERISA and the insurance industry, including the loss of PBGC insurance.
- K. Recognizing that much, if not virtually all, of today's pension information is maintained electronically, the Council intends to devote some of its time to looking at cybersecurity and cybertheft issues and how such issues might inform the Council's work in notice and disclosure in the context of risk transfer and/or how such issues might inform an area of study by a future Council.